
***KANSAS PUBLIC WATER
SUPPLY LOAN FUND
(AN ENTERPRISE FUND OF
THE STATE OF KANSAS)
FINANCIAL STATEMENTS
JUNE 30, 2011***

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Independent Auditors' Report

Dr. Robert Moser, MD
Secretary of Kansas Department of Health and Environment and the
Board of Directors of the Kansas Development Finance Authority
Topeka, Kansas

We have audited the accompanying statement of net assets of the Kansas Public Water Supply Loan Fund (the Fund), an enterprise fund of the State of Kansas, as of June 30, 2011, and the related statement of revenues, expenses and changes in net assets and cash flows for the year then ended. These financial statements are the responsibility of the Fund's management. Our responsibility is to express an opinion on these financial statements based on our audits. The financial statements of the Fund as of June 30, 2010 were audited by other auditors whose report dated October 1, 2010 expressed an unqualified opinion on those statements.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards for financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

As discussed in Note 1 to the financial statements, the financial statements referred to above present only the financial position, results of operations and cash flows of the Fund. They do not purport to and do not present fairly the financial position of the State of Kansas as of June 30, 2011 and 2010 and results of operations and its cash flows for the years then ended, in conformity with accounting principles generally accepted in the United States of America.

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the Fund as of June 30, 2011 and the results of its operations and cash flows for the year then ended, in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report dated January 27, 2012 on our consideration of the Fund's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

The accompanying management's discussion and analysis is not a required part of the financial statements but is supplementary information required by the Governmental Accounting Standards Board. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

RubinBrown LLP

Overland Park, Kansas
January 27, 2012

KANSAS PUBLIC WATER SUPPLY LOAN FUND (AN ENTERPRISE FUND OF THE STATE OF KANSAS)

MANAGEMENT'S DISCUSSION AND ANALYSIS For The Fiscal Years Ended June 30, 2011 And 2010

The Kansas Public Water Supply Loan Fund (the Fund) provides financial assistance to Kansas municipalities in the form of loans for the construction of public water supply system infrastructure. The Fund is comprised of Federal Capitalization Grants, proceeds of revenue bonds issued to provide required state-matching monies, proceeds of revenue bonds issued to leverage the program and recycled monies.

In this twelfth year of operation, the continued success of the Fund is shown below by providing project funding for the additional Public Water Supply needs of Kansas communities.

During the fiscal year ended June 30, 2011:

- FFY 2010 federal capitalization grant amendment award of \$16,605,000 was received
- Federal capitalization grant dollars drawn down: \$1,018,808 for loans, \$1,300,246 for administration and other set-aside expenses, and \$10,045,489 for American Recovery and Reinvestment Act (ARRA)
- Series 2010SRF and 2011SRF revenue bonds issued:
 - State match 2010 DW bonds issued \$2,405,000
 - Leveraged 2010 DW bonds issued \$59,105,000
 - State match 2011 DW bonds issued \$3,500,000
 - Leveraged 2011 DW bonds issued \$49,880,000
- Total available for loans-unexpended: \$7,536,326 recycled
- Total loan agreements: 217 loans totaling \$457,342,250 of which \$425,655,406 has been paid in project payments
- Loan agreements:
 - New loans \$381,720 (3 loans)
 - Declined loans \$0
 - Loan amendments: 3 increase amendments totaling \$5,440,980 and 21 decrease amendments totaling \$10,122,217
- Disbursements for project costs: \$36,405,854
- Average monthly disbursements FY2011: \$3,033,821
- Average monthly disbursements program-to-date: \$2,660,346
- Completed projects: 21 totaling: \$22,683,776
- Total revenue bond debt service paid: \$24,139,269
- Excess loan repayments and earnings: \$2,182,890

KANSAS PUBLIC WATER SUPPLY LOAN FUND

(AN ENTERPRISE FUND OF THE STATE OF KANSAS)

Management's Discussion And Analysis *(Continued)*

The Fund is reported as an enterprise fund of the State of Kansas. As such, we prepare three basic financial statements, notes to the financial statements and required supplementary information including this Management's Discussion and Analysis (MD&A). The Statements of Net Assets present the assets and liabilities of the Fund. Assets consist of cash, interest receivables from loans and investments, investments of idle funds and reserve funds, and loan receivables. Liabilities include revenue bond interest, other accounts payable, arbitrage payable, and revenue bonds payable. Net assets include the federal capitalization grants and State contribution deposited to the bond reserve account and the excess earnings of the Fund's operations since inception.

	2011	2010	2009
Current and other assets	\$ 140,914,602	\$ 81,312,246	\$ 68,149,928
Noncurrent assets	317,911,264	361,832,142	337,338,807
Total assets	458,825,866	443,144,388	405,488,735
Long-term liabilities	272,204,329	268,960,139	250,897,039
Other liabilities	20,050,084	17,079,114	16,558,553
Total liabilities	292,254,413	286,039,253	267,455,592
Restricted net assets	166,571,453	157,105,135	138,033,143
Total net assets	\$ 166,571,453	\$ 157,105,135	\$ 138,033,143

The increase in current assets for the year ended June 30, 2010, of over \$13.1 million is due in part to a net increase in cash of \$11.9 million from an increase of \$3.2 million to the general recycled loan account from the redesignation of the leveraged bond reserve, \$668,500 in excess of loan repayments over bond debt service payments, net of arbitrage rebate requirement, \$75,000 increase in general recycled loan repayments, \$9.3 million increase for leveraged project payments paid from the recycled loan account, \$923,000 decrease for recycled project payments, \$1.8 million decrease for ARRA/Recycled loan project payments that are paid from the recycled loan account, \$1.1 million increase in loan prepayments, \$109,000 decrease in the revenue interest account, \$355,000 increase in fees collected on loans, and \$19,600 increase in the ending balance of the grant set-aside accounts. Other factors include: 1) \$320,000 decrease in investment interest receivable due to the termination of the investment agreement of \$11.3 million by Westdeutsche Landmark that was not reinvested, 2) \$266,000 increase in loan interest receivable, 3) \$1.3 million increase in loan principal repayment receivable, 4) \$38,000 decrease in other receivables.

KANSAS PUBLIC WATER SUPPLY LOAN FUND (AN ENTERPRISE FUND OF THE STATE OF KANSAS)

Management's Discussion And Analysis *(Continued)*

The increase in total liabilities for the year ended June 30, 2010, of \$18.6 million was due mainly to the issuance of Series 2009 bonds of \$73,040,000 which included refunding of \$36,930,000, less debt service payments. In addition, the liability for arbitrage decreased by \$1.3 million, the loan reserve accounts held by the fund increased \$483,000, and accounts payable decreased \$82,000.

The increase in current assets for the year ended June 30, 2011 of over \$59.6 million is due in part to a net increase in cash of \$61.3 million. The 2011SRF bond issue provided \$53,000,000 in proceeds for loans. The excess of loan repayments over bond debt service payments, net of arbitrage rebate requirement provided \$2,182,890 of cash in addition to \$26.0 million from the deallocation of the leveraged bond reserve accounts. Additionally, \$38,717,608 of loan prepayments were received this fiscal year and \$33,709,341 of loan prepayments were used to partially refund outstanding revenue bonds. There was a \$183,000 decrease in the revenue interest account, a \$430,000 increase in fees collected on loans, and a \$21,000 decrease in the ending balance of the grant set-aside accounts. Other factors include: 1) \$3,000 increase in investment interest receivable 2) \$313,000 decrease in loan interest receivable, 3) \$1.4 million decrease in loan principal repayment receivable, 4) \$57,000 decrease in other receivables.

The increase in total liabilities for the year ended June 30, 2011 of \$6.2 million was due mainly to the issuance of Series 2010-1 bonds of \$61,510,000 which along with prepayments on loans provided funds to refund \$90,365,000 of previously issued bonds and the issuance of Series 2011 bonds of \$53,380,000, less debt service payments. In addition, the loan reserve accounts held by the fund decreased \$151,000, and accounts payable increased \$64,000.

Prior to the Series 2009 bonds issued on September 29, 2009, all bonds issued for this program are tax-exempt revenue bonds. The Series 2009 DW-1 bonds are tax-exempt revenue bonds and the Series 2009 DW-2 bonds are taxable Build America bonds. As a requirement for issuance of tax-exempt bonds, the Internal Revenue Service requires issuers to calculate and remit the amount of earnings attributable to the bonds that is in excess of the cost of the debt. For this Program, as of June 30, 2010, there was no rebate liability for the Series 2000, 2002, 2004, 2008, 2009 DW-1 and DW-2 bonds. As of June 30, 2011, there is no rebate liability for the Series 2002, 2004, 2008, 2009 DW-1 and DW-2, 2010-1 and 2011 bonds. The rebate liability is incrementally funded from the excess revenues available following each semiannual bond debt service payment. The Fund's revenue bonds payable totaled \$287,305,000 and \$276,465,000 at June 30, 2011 and 2010, respectively. Please refer to the notes to the financial statements for more information on debt activity.

KANSAS PUBLIC WATER SUPPLY LOAN FUND
(AN ENTERPRISE FUND OF THE STATE OF KANSAS)

Management's Discussion And Analysis *(Continued)*

The Statements of Revenues, Expenses and Changes in Net Assets provides information about the Fund resources and uses of those resources. This statement demonstrates that sufficient resources were generated to cover expenses during the fiscal year. The change in net assets as of June 30, 2010, was \$19,071,992. The Fund operating revenues increased by 9.8% due to an increase in loan interest repayments, loan origination fee and FIAC revenue, service fee revenue, interest revenue from Build America Bond subsidy payment, and grant revenue. The Fund operating expenses decreased 61.13% due to a decrease in arbitrage rebate. Nonoperating revenues decreased 59.71% due to a decrease in investment income due to the close of two investment agreements with Societe Generale and Westdeutsche Landesbank, and nonoperating expenses decreased .79% due to a decrease in bond interest expense and the amortization of bond issuance cost. \$7.7 million was drawn down from the 2008 and 2009 federal capitalization grants and deposited into the leveraged bond reserve account. The final amendment to the FFY 2009 federal capitalization grant in the amount of \$4,655,000 was awarded on September 4, 2009 and \$759,460 has not been drawn down. \$10,045,489 of the 2009 ARRA federal capitalization grant has not been drawn down.

The change in net assets as of June 30, 2011, was \$9,466,318. The Fund operating revenues increased by 3.9% due to an increase in loan origination fee and FIAC revenue and grant revenue. The Fund operating expenses (excluding principal forgiveness expense) increased 116% due to an increase in grant expenses and the change in arbitrage expenses. Nonoperating revenues decreased 34.66% due to a decrease in investment income, and nonoperating expenses decreased 8.82% due to a decrease in bond interest expense and the amortization of bond issuance cost. The FFY 2010 federal capitalization grant in the amount of \$16,605,000 was awarded on November 8, 2010 and \$15,310,627 has not been drawn down.

KANSAS PUBLIC WATER SUPPLY LOAN FUND

(AN ENTERPRISE FUND OF THE STATE OF KANSAS)

Management's Discussion And Analysis *(Continued)*

	2011	2010	2009
Revenues			
Operating revenues			
Loans	\$ 9,716,548	\$ 9,933,348	\$ 9,279,750
Grants	1,338,767	924,892	753,599
Service fees	983,393	992,153	915,901
Other	682,847	388,826	197,488
Nonoperating revenues			
Investment income			
Bond reserve fund	1,631,498	2,203,564	6,437,186
Other invested fund	336,642	808,642	1,039,962
Total Revenues	14,689,695	15,251,425	18,623,886
Expenses			
Operating expenses			
Program administration - federal	467,189	361,287	385,160
Other program set-asides	910,824	540,349	393,817
Program administration - other	683,896	620,610	726,877
Arbitrage rebate	—	(567,756)	1,453,372
Loan principal forgiveness	3,109,235	195,900	—
Nonoperating expenses			
Bond issuance costs amortized	195,802	216,086	288,992
Bond interest	10,920,728	11,975,543	11,999,920
Total Expenses	16,287,674	13,342,019	15,248,138
Decrease in net assets			
Before contributions	(1,597,979)	1,909,406	3,375,748
Capital contributions			
Capitalization grants - ARRA	10,045,489	9,454,511	—
Capitalization grants, net of recognized administrative grants	1,018,808	7,708,075	7,059,825
Increase in net assets	9,466,318	19,071,992	10,435,573
Total net assets - beginning of year	157,105,135	138,033,143	127,597,570
Total net assets - end of year	\$ 166,571,453	\$ 157,105,135	\$ 138,033,143

The Statements of Cash Flows are provided to identify the sources and the uses of cash during the fiscal year and to demonstrate that the Fund has sufficient cash to meet its obligations. As of June 30, 2010, the Fund experienced a net increase in cash of \$33,595,626. This increase is from the net proceeds from the Series 2009 bond issue. The balance of the increase is due to routine Program operations.

During the year ended June 30, 2011, the Fund experienced a net increase in cash of \$35,198,451. Part of this increase is from the net proceeds from the Series 2011 bond issue. The balance of the increase is due to routine Program operations.

This report is intended to provide financial information about the Kansas Public Water Supply Loan Fund to State of Kansas and United States Environmental Protection Agency officials, investors and other interested parties and to discuss the activity and success of the Fund. For additional information you may contact William Carr, Program Coordinator, Kansas Department of Health and Environment or Roger Basinger, Office of Management Analysis and Standards Section Manager, Department of Administration.

KANSAS PUBLIC WATER SUPPLY LOAN FUND (AN ENTERPRISE FUND OF THE STATE OF KANSAS)

STATEMENTS OF NET ASSETS

	June 30,	
	2011	2010
Assets		
Current assets:		
Cash	\$ 122,077,513	\$ 60,737,839
Investment interest receivable	467,604	464,604
Loan interest receivable	3,907,531	4,220,954
Loans	13,906,142	15,275,722
Other receivables	555,812	613,127
Total current assets	140,914,602	81,312,246
Noncurrent assets:		
Restricted cash - arbitrage rebate	—	100,000
Restricted cash - loan reserve earnings	12,726	41,440
Loans	263,795,392	281,466,874
Loan reserve accounts	8,089,538	8,207,283
Debt service reserve funds - investments	23,202,588	23,202,588
Debt service reserve funds - cash	19,901,162	45,913,671
Bond issue costs, net of amortization	2,909,858	2,900,286
Total noncurrent assets	317,911,264	361,832,142
Total Assets	458,825,866	443,144,388
Liabilities		
Current liabilities		
Accounts payable and accrued expenses	244,233	180,578
Bond interest payable	3,580,851	3,213,536
Revenue bonds payable, current	16,225,000	13,685,000
Total current liabilities	20,050,084	17,079,114
Noncurrent liabilities		
Loan reserve accounts payable	8,102,815	8,254,214
Revenue bonds payable, long-term, net	281,601,338	269,485,488
Deferred amounts on refunding	(17,499,824)	(8,779,563)
Total noncurrent liabilities	272,204,329	268,960,139
Total Liabilities	292,254,413	286,039,253
Net Assets		
Restricted net assets	166,571,453	157,105,135
Total Net Assets	\$ 166,571,453	\$ 157,105,135

KANSAS PUBLIC WATER SUPPLY LOAN FUND (AN ENTERPRISE FUND OF THE STATE OF KANSAS)

STATEMENTS OF REVENUES, EXPENSES AND CHANGES IN NET ASSETS

	For The Years Ended June 30,	
	2011	2010
Operating Revenues		
Interest on loans	\$ 9,716,548	\$ 9,933,348
Grant revenue	1,338,767	924,892
Service fee revenue	983,393	992,153
Other revenue	682,847	388,826
Total Operating Revenues	12,721,555	12,239,219
Operating Expenses		
Program administration - federal	467,189	361,287
Program administration - other federal set-asides	910,824	540,349
Program administration - other	683,896	620,610
Arbitrage rebate	—	(567,756)
Loan principal forgiveness	3,109,235	195,900
Total Operating Expenses	5,171,144	1,150,390
Operating Income	7,550,411	11,088,829
Nonoperating Revenues (Expenses)		
Investment income		
Bond reserve fund	1,631,498	2,203,564
Other investment income	336,642	808,642
Capital contributions - capitalization grants net of recognized administrative grants	1,018,808	7,708,075
Capital contributions - ARRA capitalization grants, net of recognized administrative grants	10,045,489	9,454,511
Bond issuance costs - amortization	(195,802)	(216,086)
Interest expense - bonds	(10,920,728)	(11,975,543)
Total Nonoperating Revenues (Expenses)	1,915,907	7,983,163
Change In Net Assets	9,466,318	19,071,992
Net Assets - Beginning Of Year	157,105,135	138,033,143
Total Net Assets - End Of Year	\$ 166,571,453	\$ 157,105,135

KANSAS PUBLIC WATER SUPPLY LOAN FUND (AN ENTERPRISE FUND OF THE STATE OF KANSAS)

STATEMENTS OF CASH FLOWS

	For The Years Ended June 30,	
	2011	2010
Cash Flows From Operating Activities		
Loan principal collected	\$ 52,337,681	\$ 17,007,924
Loans disbursed	(36,405,854)	(38,030,964)
Interest received on loans	10,029,970	9,667,126
Program administration expenses	(1,378,013)	(901,635)
Arbitrage rebate paid	—	(734,863)
Other revenue	747,561	245,635
Service fees received	1,007,752	961,040
Service fees paid	(651,999)	(566,064)
Capitalization grant for administrative costs	1,338,767	924,892
Net Cash Provided By (Used In) Operating Activities	27,025,865	(11,426,909)
Cash Flows From Noncapital Financing Activities		
Bond principal paid	(13,685,000)	(13,620,000)
Bond interest paid	(10,454,269)	(12,153,141)
ARRA capitalization grant for loans	10,045,489	9,454,511
Capitalization grant for reserve fund	1,018,808	7,708,075
Bond proceeds, including premium	122,851,953	72,952,223
Payment to bond escrow agent	(102,029,852)	(39,169,488)
Bond issuance costs paid	(1,506,031)	(660,013)
Net Cash Provided By Noncapital Financing Activities	6,241,098	24,512,167
Cash Flows From Investing Activities		
Proceeds from sales and maturities of debt service reserve funds	—	17,249,825
Interest received on investments and debt service reserve funds	1,965,142	3,331,950
Net purchases of investments in loan reserve accounts	(33,654)	(71,407)
Net Cash Provided By Investing Activities	1,931,488	20,510,368
Net Increase In Cash	35,198,451	33,595,626
Cash – Beginning Of Year	106,792,950	73,197,324
Cash – End Of Year	\$ 141,991,401	\$ 106,792,950
Cash consists of:		
Cash	\$ 122,077,513	\$ 60,737,839
Debt service reserve fund - cash	19,901,162	45,913,671
Restricted cash - arbitrage rebate	—	100,000
Restricted cash - loan reserve earnings	12,726	41,440
	\$ 141,991,401	\$ 106,792,950
Reconciliation Of Operating Income To Net Cash Provided By (Used In) Operating Activities		
Operating income	\$ 7,550,411	\$ 11,088,829
Adjustments to reconcile operating income to net cash provided by (used in) operating activities:		
Loans receivable	19,041,061	(20,827,140)
Loan interest receivable	313,423	(266,222)
Other receivables	57,315	(38,010)
Accounts payable and accrued expenses	63,655	(81,747)
Arbitrage rebate payable	—	(1,302,619)
Net Cash Provided By (Used In) Operating Activities	\$ 27,025,865	\$ (11,426,909)

KANSAS PUBLIC WATER SUPPLY LOAN FUND (AN ENTERPRISE FUND OF THE STATE OF KANSAS)

NOTES TO FINANCIAL STATEMENTS

June 30, 2011 And 2010

1. Organization And Summary Of Accounting Policies

Description Of Program

The Kansas Public Water Supply Loan Fund (the Fund) was established pursuant to Kansas Statutes Annotated (K.S.A.) 65-163d et. seq. in 1994 by the Kansas Legislature. The Fund was created to implement the State of Kansas' (Kansas or the State) participation under the Federal Safe Drinking Water Act (the Federal Act) as amended by the Safe Drinking Water Act Amendments of 1996. Under Kansas law, the Secretary of the Kansas Department of Health and Environment (KDHE) administers the Public Water Supply Loan Program (the Program). The Federal Act authorizes the Environmental Protection Agency (EPA) to award capitalization grants for deposit into state funds in order to provide financial assistance for construction and management of public water supply systems. The Program is the response by the State to federal law changes governing the development of publicly owned, public water supply systems including the financing, construction and management of those systems. The state fund may be used to make loans, fund debt service reserves and provide other types of financial assistance to public entities. Initial funding for the Program is to be provided by the EPA capitalization grants and proceeds of bonds which will provide State match funds. The State match funds must be equal to 20% of the federal capitalization grants. The Fund is to be established, maintained and credited with loan repayments and the Fund equity is to be available in perpetuity for providing such financial assistance. The capitalization grants are included within the scope of the State of Kansas OMB Circular A-133 single audit.

Loans are made to municipalities, as defined by the K.S.A., from the Fund for eligible project costs. Kansas Administrative Regulation 28-15-52 established the interest rates for the loans, together with fees set for servicing the loans, to be an amount equal to 60% of the previous three months' average "bond buyers 20 bond index" as published each week of the preceding three months. KDHE administers the aspects of the Program relating to selection of projects and the making of loans to eligible municipalities. The Department of Administration administers the accounting and reporting aspects of the Program relating to the receipt and disbursement of monies within the Fund including disbursement of loans to municipalities and billing and collecting of loan repayments. The Kansas Development Finance Authority (KDFA) issues revenue bonds for the State matching funds needed and for leveraged borrowing for the Fund. Monies in the Fund are deposited with the Treasurer of the State of Kansas (the Treasurer) and UMB (the Trustee).

KANSAS PUBLIC WATER SUPPLY LOAN FUND (AN ENTERPRISE FUND OF THE STATE OF KANSAS)

Notes To Financial Statements *(Continued)*

Basis Of Presentation

The Fund is an enterprise fund of the State. In reporting its financial activity, the Fund has elected to apply applicable Financial Accounting Standards Board Statements and Interpretations issued prior to November 30, 1989. The Fund has elected not to follow subsequent private-sector guidance.

Basis Of Accounting

The financial statements of the Fund have been prepared in conformity with accounting principles generally accepted in the United States of America as applied to government units. The Governmental Accounting Standards Board (GASB) is the accepted standard-setting body for establishing governmental accounting and financial reporting principles.

Basis of accounting refers to when revenues, expenses and the related assets and liabilities are recognized in the accounts and reported in the financial statements. Measurement focus refers to what is being measured. The financial statements are prepared on the accrual basis of accounting and on an economic resources measurement focus in accordance with accounting principles generally accepted in the United States of America. With this measurement focus, all assets and all liabilities are included on the statement of net assets. The statement of revenues, expenses, and changes in fund net assets presents increases (revenues) and decreases (expenses) in net total assets. The statement of cash flows provides information about how the Fund meets the cash flow needs of its activities.

Cash

Cash includes balances on deposit with the Treasurer and the Trustee.

Investments

The Fund generally invests in investment agreements and repurchase agreements. These investments are stated at cost as they are not negotiable or transferable and are not affected by market fluctuations.

Loans And Other Receivables

Receivables include interest earnings, current loan repayments due and loan principal balances outstanding. All receivables are considered collectable; therefore, no allowance account has been established.

KANSAS PUBLIC WATER SUPPLY LOAN FUND (AN ENTERPRISE FUND OF THE STATE OF KANSAS)

Notes To Financial Statements *(Continued)*

Loan Reserve Accounts

The loan reserve accounts have been established as required under certain provisions of certain loan agreements and consist of cash. Such loan reserve accounts may only be used to prevent any event of default in the repayment of principal or interest on certain loans.

Debt Service Reserve Account

The debt service reserve account was established as required under certain bond resolutions and consists of investments in investment agreements and repurchase agreements. The investments are stated at cost as they are not negotiable or transferable and are not affected by market fluctuations. No trustee is required by the bond resolutions. Contractually, such investments may only be used to prevent any default in the payment of principal or interest on bonds payable.

Bond Issuance Costs, Premiums And Discounts - Bond issuance costs are being amortized over the life of the bonds using the straight-line method. Beginning with the 2002 bonds, the interest method is being used to calculate amortization of premium and discount. Prior to the 2002 issue premium and discount are being amortized on the straight-line method.

Revenues - The Fund revenues consist of operating and nonoperating revenues. Operating revenues include: 1) interest earned on loans, 2) federal grant dollars earned for administrative costs, also known as program set-asides (program administration, technical assistance, state program management, and other authorized activities 1452K (1)b, and 3) loan service fees earned. Nonoperating revenues include the investment income on bond reserves and other invested program monies and any other revenues not classified as operating revenues.

Expenses - The Fund expenses consist of operating and nonoperating expenses. Operating expenses include: 1) federal grant monies for administrative costs, also known as program set-asides (program administration, technical assistance, state program management, and other authorized activities 1452K (1)b, and 2) amounts due to the IRS for arbitrage rebate on program revenue bonds. Nonoperating expenses include: 1) revenue bond interest, 2) revenue bond issuance costs amortized and 3) revenue bond premium and discount amortized.

KANSAS PUBLIC WATER SUPPLY LOAN FUND (AN ENTERPRISE FUND OF THE STATE OF KANSAS)

Notes To Financial Statements *(Continued)*

Net Assets

Net assets represent the difference between assets and liabilities. Net assets invested in capital assets, net of related debt, consists of capital assets, net of accumulated depreciation, reduced by the outstanding balances of any borrowings used for the acquisition, construction or improvement of those assets. Currently the fund has no net assets invested in capital assets. Net assets are reported as restricted when there are external limitations imposed on their use. All assets of the program have been determined to be restricted assets in accordance with the conditions of the Public Water Supply EPA capitalization grants and bond covenants. Restricted net assets include EPA capitalization grants restricted for the 1) bond reserve fund, 2) loans to municipalities, 3) program administration expenses, 4) technical assistance, 5) state program management, 6) and other authorized activities 1452K (1)b. The amount of capitalization grants restricted for program administration, technical assistance, state program management, and other authorized activities 1452K (1)b is being recognized as revenue when earned. Also included in restricted net assets is an account titled "Contributed Capital - State of Kansas." The account consists of monies contributed to the Fund per K.S.A. 74-8203, as amended and supplemented.

Use Of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

KANSAS PUBLIC WATER SUPPLY LOAN FUND (AN ENTERPRISE FUND OF THE STATE OF KANSAS)

Notes To Financial Statements *(Continued)*

2. Investments And Debt Service Reserve Accounts

The Fund's investment policies are governed by Article IX of the Master Bond Resolution and Article VIII of the Master Financing Indenture. Allowable investments for the Fund cash balances held in the State Treasury and invested through the State Pooled Money Investment Board are as follows:

- Direct obligations of, or obligations that are insured as to principal and interest by, the U.S. Government or any direct agency thereof, with maturities up to four years
- Repurchase agreements with Kansas banks or with primary government securities dealers
- Limited interest bearing loans to various State agencies as specifically provided by law
- Certain Kansas agency and IMPACT Act projects and bonds
- High grade commercial paper

Specific Fund Investments - Cash balances not held in the State Treasury may be invested as permitted by bond documents and bond covenants. Allowable investments include:

- U.S. Government obligations
- Obligations of government-sponsored agencies
- Federal funds, unsecured certificates of deposit, time deposits and banker's acceptances
- Deposits fully insured by FDIC
- Commercial paper
- Investments in money market funds
- Repurchase agreements
- Stripped securities
- Investments in the Municipal Investment Pool Fund
- Investment agreements
- Guaranteed investment contracts

Monies held in the Funds and Accounts established under the Master Financing Indenture may be invested by the KDFA or by the Trustee to the fullest extent practicable in Investment Securities as defined in the Master Financing Indenture which include:

KANSAS PUBLIC WATER SUPPLY LOAN FUND
(AN ENTERPRISE FUND OF THE STATE OF KANSAS)

Notes To Financial Statements *(Continued)*

- Defeasance obligations
- Obligations of certain nonfull faith and credit U.S. government agencies
- Investments in money market funds
- Investment agreements
- Deposits-fully insured by FDIC
- Commercial paper
- State or municipal debt obligations
- Investments in the Municipal Investment Pool Fund
- Repurchase agreements
- Guaranteed investment contracts

As of June 30, 2011 and 2010, respectively, the program's investment and debt service reserve account balances were as follows:

Investment Type	Carrying Value	Less Than 1 Year	1 - 5 Years	6 - 10 Years	More Than 10 Years
Repurchase agreements	\$ 9,827,552	\$ —	\$ —	\$ —	\$ 9,827,552
Investment agreements	13,375,036	—	—	—	13,375,036
	\$ 23,202,588	\$ —	\$ —	\$ —	\$ 23,202,588

Investment Type	Carrying Value	Less Than 1 Year	1 - 5 Years	6 - 10 Years	More Than 10 Years
Repurchase agreements	\$ 9,827,552	\$ —	\$ —	\$ —	\$ 9,827,552
Investment agreements	13,375,036	—	—	—	13,375,036
	\$ 23,202,588	\$ —	\$ —	\$ —	\$ 23,202,588

The investments shown above represent debt service reserve accounts.

Interest Rate Risk - Due to the tax exempt status of the bonds it is generally the practice of Fund management to match reserve fund interest rates to the arbitrage yield on the bonds and the term of the investments to the maturity of the bonds. For invested loan funds, the Fund generally invests to maximize the interest rate and set a term of investment based on estimated expenditures which is generally 3 – 5 years.

Credit Risk - The Fund holds investments that may have credit risk since the underlying securities may include securities other than those that take the form of U.S. Treasuries or obligations explicitly guaranteed by the U.S. government. The investments are unrated. Certain investments have an underlying collateral agreement.

KANSAS PUBLIC WATER SUPPLY LOAN FUND
(AN ENTERPRISE FUND OF THE STATE OF KANSAS)

Notes To Financial Statements *(Continued)*

Concentration of Credit Risk - The Fund places no limit on the amount that may be invested with any one provider. The table below identifies the percent of total investments held by each provider as of June 30, 2011.

Investment Provider	Fair Value	Percent Of Total
Citigroup	\$ 9,827,552	42.36%
AIG	13,375,036	57.64%
	\$ 23,202,588	100.00%

3. Loans

The loans made by the Fund to the municipalities may include interest and service fees capitalized during project construction. Loans are to be repaid not later than twenty years after project completion. Principal and interest payments are due semi-annually. Interest rates on the loans outstanding at June 30, 2011, excluding the .35% service fee rate, range from 2.98% to 4.42%.

Commitments to municipalities participating in the Program and outstanding loan balances as of June 30 are as follows:

Project	2011 Total Loan Commitment	2011 Cumulative Amount Loaned	2011 Undisbursed Loan Commitment	2011 Outstanding Loan Balance	2010 Outstanding Loan Balance
Abilene	\$ 1,400,000	\$ 1,400,000	\$ —	\$ 684,389	\$ 755,744
Alma	481,206	481,206	—	251,925	274,592
Almena	615,500	615,500	—	496,036	519,979
Arkansas City	1,650,000	1,140,606	509,394	1,113,433	810,255
Arlington	526,729	526,729	—	478,565	498,318
Assaria	489,000	489,000	—	319,851	341,688
Atchison	3,834,075	3,455,815	378,260	3,455,815	545,983
Baldwin City	1,599,236	1,599,236	—	1,198,586	1,264,987
Baxter Springs	2,900,000	2,900,000	—	1,942,703	2,072,102
Bentley	480,000	336,960	143,040	336,960	138,243
Blue Rapids	416,300	208,066	208,234	208,066	40,541
Brown Co. RWD #2	130,047	130,047	—	—	125,467
Buhler	2,038,095	1,074,280	963,815	1,074,280	23,447
Burlington	5,059,982	5,059,982	—	3,726,967	3,923,978
Butler Co. RWD #5	400,000	400,000	—	364,383	379,009
Butler Co. RWD #8	816,871	816,871	—	511,099	549,219
Caney	1,344,167	1,344,167	—	1,214,443	1,275,648
Carbondale	1,350,460	1,350,460	—	730,639	780,145
Carbondale 2	2,617,294	2,617,294	—	2,153,634	2,258,752
Chanute	1,750,000	1,750,000	—	1,205,438	1,281,794
Chanute 2	632,557	632,557	—	514,016	539,428
Chanute 3	147,020	—	147,020	—	—
Cheney	601,494	601,494	—	546,682	566,765
Cherokee Co. RWD #3	1,738,382	1,738,382	—	1,509,475	1,575,349
Cherryvale	813,270	699,377	113,893	689,167	643,050
Chetopa	1,624,416	1,624,416	—	1,192,157	1,263,176
Cimarron	1,511,421	1,511,421	—	856,936	929,622

KANSAS PUBLIC WATER SUPPLY LOAN FUND

(AN ENTERPRISE FUND OF THE STATE OF KANSAS)

Notes To Financial Statements *(Continued)*

Project	2011 Total Loan Commitment	2011 Cumulative Amount Loaned	2011 Undisbursed Loan Commitment	2011 Outstanding Loan Balance	2010 Outstanding Loan Balance
Clay Center	9,800,000	9,608,634	191,366	8,740,672	8,162,464
Clay Co. RWD #2	256,013	256,013	—	232,875	241,695
Cloud Co. RWD #1	435,867	435,867	—	353,987	370,972
Coffeyville 1	2,443,456	2,443,456	—	1,668,300	1,771,045
Coffeyville 2	418,391	418,391	—	287,050	305,059
Coffeyville 3	467,436	467,436	—	363,281	382,073
Coffeyville 4	663,935	663,935	—	478,433	—
Colwich	3,576,879	3,576,879	—	—	2,518,228
Copeland	63,000	—	63,000	—	—
Council Grove	2,258,481	2,258,481	—	1,746,441	1,835,821
Crawford Co. RWD #5	579,651	579,651	—	333,639	358,390
Crawford Co. RWD #7	99,466	99,466	—	80,893	84,841
Dodge City	4,394,239	4,394,239	—	2,663,987	2,831,122
Doniphan Co. RWD #5	46,304	46,304	—	—	—
Douglas Co. RWD #2	749,183	749,183	—	353,852	732,282
Douglas Co. RWD #3	5,576,450	2,873,728	2,702,722	2,767,754	2,873,728
Douglas Co. RWD #4	857,696	857,696	—	630,544	666,688
Douglas Co. RWD #5	1,158,095	1,158,095	—	558,347	595,028
Douglass	65,843	65,843	—	56,079	58,649
Downs	436,873	436,873	—	355,443	372,910
Edgerton	1,141,617	1,141,617	—	725,901	777,399
Effingham	740,813	740,813	—	691,945	720,824
Ellsworth	2,041,438	2,041,438	—	—	1,492,725
Emporia	4,739,011	4,739,011	—	—	2,851,402
Emporia 2	2,423,971	2,423,971	—	1,657,988	1,156,008
Eureka	450,000	450,000	—	258,369	280,141
Eureka 2	2,106	2,106	—	—	—
Finney Co. RWD #1	2,511,217	2,511,217	—	1,362,619	1,494,239
Florence	155,316	155,316	—	104,247	110,227
Fort Scott	2,169,247	2,169,247	—	1,635,141	1,716,104
Fort Scott 2	5,480,086	5,480,086	—	4,255,124	4,471,641
Frontenac	1,882,000	586,597	1,295,403	313,485	353,806
Galena	165,000	105,893	59,107	101,996	—
Garden City	5,678,100	5,678,100	—	—	3,151,154
Garden City 2	2,614,133	2,614,133	—	—	2,016,640
Gardner	7,582,910	7,582,910	—	5,382,885	5,640,842
Garnett	1,200,694	1,200,694	—	846,980	898,175
Garnett 2	1,100,000	616,728	483,272	616,728	236,075
Geary Co. RWD #4	383,965	383,965	—	295,872	311,891
Glen Elder	139,896	139,896	—	124,326	129,689
Goessel	340,902	340,902	—	235,576	250,355
Goodland	2,480,050	2,480,050	—	1,337,029	1,457,702
Goodland 2	6,015,038	5,427,259	587,779	5,427,259	2,064,767
Grainfield	84,663	84,663	—	75,044	78,051
Hanover	71,766	71,766	—	—	—
Harper Co. RWD #2	549,064	549,064	—	425,020	447,650
Harvey Co. RWD #1	539,677	539,677	—	295,260	322,033
Harvey Co. RWD #1-2	3,703,632	3,703,632	—	3,314,365	3,451,576
Herington	1,222,806	1,222,806	—	1,017,761	1,065,725
Hesston	1,631,806	1,631,806	—	1,493,185	1,551,410
Hiawatha	702,737	702,737	—	372,605	393,964
Hill City	2,360,731	2,360,731	—	2,097,882	2,187,413
Hill City 2	421,125	314,894	106,231	314,894	—
Hillsboro	146,352	146,352	—	119,296	125,119
Holton	357,605	357,605	—	304,397	318,396
Holyrood	262,259	262,259	—	212,916	223,478
Hoyt	814,697	814,697	—	532,943	569,790
Hutchinson	1,403,530	1,403,530	—	894,865	945,782
Hutchinson 2	6,666,667	6,666,667	—	5,832,132	6,078,874

KANSAS PUBLIC WATER SUPPLY LOAN FUND

(AN ENTERPRISE FUND OF THE STATE OF KANSAS)

Notes To Financial Statements *(Continued)*

Project	2011 Total Loan Commitment	2011 Cumulative Amount Loaned	2011 Undisbursed Loan Commitment	2011 Outstanding Loan Balance	2010 Outstanding Loan Balance
Independence	2,500,000	1,499,582	1,000,418	1,444,064	246,862
Ingalls	155,346	155,346	—	112,772	119,072
Iola	10,000,000	10,000,000	—	7,773,670	8,180,702
Jackson Co. RWD #1	2,170,441	2,170,441	—	932,032	983,379
Jackson Co. RWD #3	995,324	975,391	19,933	891,903	466,284
Jefferson Co. RWD #13	2,360,113	2,360,113	—	1,773,889	1,506,470
Jewell Co. RWD #1	27,488	27,488	—	—	—
Johnson Co. Consolidated RWD #6	1,239,437	1,239,437	—	634,846	696,168
Johnson Co. RWD #7	1,578,591	1,578,591	—	865,734	943,629
Johnson Co. RWD #7-2	635,642	635,642	—	489,922	516,426
Johnson Co. RWD #7-3	957,747	957,747	—	866,175	900,874
Johnson Co. RWD #7-4	171,700	—	171,700	—	—
Junction City	744,293	744,293	—	456,539	488,103
Junction City 2	800,000	340,841	459,159	321,252	50,800
Kansas City BPU 1	12,308,750	12,308,750	—	8,955,017	9,450,356
Kansas City BPU 2	5,118,465	5,118,465	—	3,750,832	3,958,625
Kansas City BPU 3	9,000,000	9,000,000	—	7,648,549	7,998,418
Kirwin	304,000	203,040	100,960	203,040	84,366
Kismet	159,714	159,714	—	144,684	150,674
LaCrosse	326,318	326,318	—	—	280,983
Lakin	3,400,000	452,815	2,947,185	452,815	—
Lane	389,000	137,185	251,815	61,723	86,383
Lawrence	6,167,307	6,167,307	—	—	4,396,895
Lawrence 2	5,562,864	5,562,864	—	—	4,178,131
Leavenworth Co. Consolidated RWD #1	2,964,361	2,964,361	—	443,628	638,709
Leavenworth Co. Consolidated RWD #1-2	430,237	430,237	—	390,912	407,047
Leavenworth Co. RWD #7	1,652,957	1,652,957	—	1,176,967	1,247,754
Leavenworth Co. RWD #9	809,347	809,347	—	—	—
Leavenworth Waterworks Board	6,972,442	6,972,442	—	1,690,180	2,799,727
Liberal	5,607,992	5,607,992	—	3,652,561	3,842,744
Little River	520,840	124,143	396,697	124,143	—
Logan	650,000	650,000	—	351,304	381,102
Long Island	188,741	188,741	—	130,390	138,626
Lyon Co. RWD #1	445,408	445,408	—	—	—
Maize	5,300,000	5,300,000	—	—	—
Manhattan	17,975,861	8,824,999	9,150,862	8,824,999	—
Marion Co. Improvement District #2	526,799	526,799	—	524,554	297,586
Marion Co. RWD #1	328,522	328,522	—	236,601	249,410
Marion Co. RWD #4	1,844,781	1,844,781	—	—	—
Marshall Co. RWD #3	575,465	575,465	—	—	—
Marshall Co. RWD #3-2	580,336	580,336	—	354,357	380,321
Marysville	301,747	301,747	—	214,093	226,942
Marysville 2	2,008,008	2,008,008	—	1,972,075	1,552,454
McLouth	1,009,840	1,009,840	—	485,265	535,094
Medicine Lodge	587,533	587,533	—	397,959	423,288
Medicine Lodge 2	326,090	326,090	—	314,542	326,090
Miami Co. RWD #2	5,515,053	5,515,053	—	—	3,302,081
Minneapolis	2,515,453	2,515,453	—	2,069,028	2,167,053
Moran	234,664	234,664	—	203,864	212,031
Nemaha Co. RWD #3	1,149,928	1,149,928	—	971,418	1,013,969
Nemaha Co. RWD #3.2	3,291,615	3,291,615	—	2,444,066	825,910
Ness City	1,101,803	1,101,803	—	894,018	936,225
New Strawn	1,269,789	1,269,789	—	854,021	909,575
Newton	2,086,456	2,086,456	—	1,031,060	1,137,621
Newton 2	1,231,500	1,231,500	—	768,101	837,749
Newton 3	1,749,683	1,749,683	—	1,635,731	1,699,663
Newton 4	651,533	651,533	—	566,047	587,772
Nickerson	332,289	332,289	—	301,887	314,347
North Newton	590,920	590,920	—	444,129	468,942

KANSAS PUBLIC WATER SUPPLY LOAN FUND

(AN ENTERPRISE FUND OF THE STATE OF KANSAS)

Notes To Financial Statements *(Continued)*

Project	2011 Total Loan Commitment	2011 Cumulative Amount Loaned	2011 Undisbursed Loan Commitment	2011 Outstanding Loan Balance	2010 Outstanding Loan Balance
Norton	4,111,316	4,111,316	—	1,506,830	3,602,821
Olathe	20,000,000	20,000,000	—	18,848,389	19,047,360
Olathe 2	16,876,745	16,876,745	—	15,789,133	16,092,880
Olathe 3	230,875	230,875	—	150,821	156,995
Osage City	2,711,274	2,711,274	—	1,966,436	2,078,739
Osage Co. RWD #3	500,000	500,000	—	234,834	246,685
Osage Co. RWD #4	250,000	250,000	—	199,968	209,910
Osage Co. RWD #5	1,079,772	1,079,772	—	742,781	572,072
Osawatomie	901,479	901,479	—	607,291	645,496
Osborne	276,505	276,505	—	165,865	179,051
Ottawa 1	989,003	989,003	—	920,715	802,429
Overbrook	160,000	160,000	—	111,730	118,431
Parsons	9,200,000	9,200,000	—	4,777,222	5,208,834
Parsons 2	5,000,000	5,000,000	—	4,700,475	4,725,192
Phillipsburg	920,980	920,980	—	630,136	644,900
Pittsburg	8,737,424	4,841,521	3,895,903	4,613,737	518,459
Pleasanton	610,692	610,692	—	491,697	516,005
Pottawatomie Co. RWD #3	479,215	479,215	—	347,596	367,624
Potwin	145,000	145,000	—	115,228	121,105
Pratt	1,292,927	722,223	570,704	629,769	81,232
Public Wholesale Water Supply Dist. #4	1,124,154	1,124,154	—	556,113	613,801
Public Wholesale Water Supply Dist. #4-2	530,710	530,710	—	178,592	307,155
Public Wholesale Water Supply Dist. #4-3	897,114	897,114	—	850,760	881,954
Public Wholesale Water Supply Dist. #17	3,334,455	3,334,455	—	1,955,986	2,128,361
Ransom	853,670	853,670	—	713,208	746,173
Reno Co. RWD #1	90,000	—	90,000	—	—
Riley	832,124	832,124	—	810,177	523,956
Rolla	241,577	241,577	—	236,715	210,613
Rush Center	67,736	67,736	—	—	—
Russell	1,675,000	1,675,000	—	871,987	951,055
Russell 2	6,012,444	6,012,444	—	5,155,697	5,379,427
Russell 3	403,707	403,707	—	276,932	281,687
Salina	3,600,000	3,600,000	—	—	2,174,635
Salina 2	5,000,000	5,000,000	—	—	3,685,742
Saline Co. RWD #4	33,803	33,803	—	—	—
Scammon	110,284	84,916	25,368	75,098	80,068
Sedgwick Co. RWD #2	1,050,376	1,050,376	—	969,109	1,007,190
Seneca	1,105,803	1,105,803	—	1,006,676	1,045,729
Seneca 2	305,653	305,653	—	229,830	208,436
Severy	143,624	143,624	—	85,101	92,010
Sharon Springs	499,616	499,616	—	275,266	301,502
Shawnee Co. RWD #1C	3,595,595	3,595,595	—	2,357,419	2,511,478
Shawnee Co. RWD #3	915,770	915,770	—	503,756	549,222
Shawnee Co. RWD #4	12,422,182	12,422,182	—	11,739,382	12,172,569
Spivey	78,000	78,000	—	—	—
Spring Hill	1,835,090	1,835,090	—	1,420,281	1,496,023
St. George	491,956	491,956	—	377,363	397,794
St. Marys	546,673	546,673	—	507,325	527,250
Sterling	488,176	488,176	—	230,086	257,085
Stockton	2,800,000	2,800,000	—	—	—
Strong City	289,815	289,815	—	159,726	170,631
Sylvan Grove	160,902	160,902	—	83,959	92,112
Tonganoxie	3,007,519	1,972,924	1,034,595	1,972,924	—
Topeka 1	7,823,725	7,823,725	—	6,340,599	6,639,942
Topeka 2	2,055,933	2,055,933	—	1,704,043	1,785,060
Topeka 3	3,127,353	3,127,353	—	2,659,055	2,776,079
Topeka 4	1,545,025	1,545,025	—	1,339,157	1,426,310
Topeka 5	3,619,009	—	3,619,009	—	—
Topeka 6	2,027,074	2,027,074	—	1,561,028	1,687,421

KANSAS PUBLIC WATER SUPPLY LOAN FUND
(AN ENTERPRISE FUND OF THE STATE OF KANSAS)

Notes To Financial Statements *(Continued)*

Project	2011 Total Loan Commitment	2011 Cumulative Amount Loaned	2011 Undisbursed Loan Commitment	2011 Outstanding Loan Balance	2010 Outstanding Loan Balance
Udall	1,365,000	1,365,000	—	1,314,108	1,365,000
Ulysses	194,707	194,707	—	128,016	136,571
Valley Center	2,934,674	2,934,674	—	1,383,113	1,516,712
Valley Center 2	1,130,797	1,130,797	—	1,008,344	1,050,634
Valley Falls	323,767	323,767	—	275,148	288,137
Victoria	465,456	465,456	—	404,475	192,376
White City	599,777	599,777	—	500,088	522,961
Wichita	7,220,000	7,220,000	—	4,581,984	4,913,006
Wilson	351,275	351,275	—	313,796	326,032
Winfield	2,330,986	2,330,986	—	—	1,671,078
Winfield 2	6,042,120	6,042,120	—	—	5,039,228
Woodson Co. RWD #1	500,000	500,000	—	241,794	253,396
Yates Center	576,897	576,897	—	426,050	—
	\$ 457,342,250	\$ 425,655,406	\$ 31,686,844	\$ 277,701,534	\$ 296,742,596

Certain of the above loans are funded from the American Recovery and Reinvestment Act (ARRA) monies. Principal forgiveness totaled \$3,109,235 and \$195,900 as of June 30, 2011 and 2010, respectively, with a cumulative amount of principal forgiveness of \$3,305,135 on 12 loans.

Each of the above municipalities has established a dedicated source of revenue for repayment of the loans. The dedicated sources of revenue are either an obligation of system revenues and ad valorem property taxes levied or a secured lien on the system revenues which requires a debt service coverage of 125% with a 10% reserve account or a debt service coverage of 140%.

4. Loan Reserve Accounts

Loan reserve accounts for forty-three Rural Water Districts and five municipalities total \$8,089,538 and \$8,207,283 as of June 30, 2011 and 2010, respectively, with restricted cash earnings of \$12,726 and \$41,440, respectively. The balances are on deposit with the State Treasurer.

KANSAS PUBLIC WATER SUPPLY LOAN FUND
(AN ENTERPRISE FUND OF THE STATE OF KANSAS)

Notes To Financial Statements *(Continued)*

5. Revenue Bonds Payable

Revenue bonds payable consisted of the following at June 30:

	2011	2010
2002 Series 1 Revenue Bonds (State Match Bonds)	\$ 175,000	\$ 2,840,000
2002 Series 2 Revenue Bonds (Leveraged Bonds)	1,950,000	17,650,000
2004 Series 1 Revenue Bonds (State Match Bonds)	5,269,000	5,845,000
2004 Series 2 Revenue Bonds (Leveraged Bonds)	93,366,000	143,055,000
2008 Series 1 Revenue Bonds (State Match Bonds)	2,050,000	3,415,000
2008 Series 2 Revenue Bonds (Leveraged Bonds)	160,000	31,700,000
2009 Series DW-1 Revenue Bonds (State Match Bonds)	6,400,000	6,720,000
2009 Series DW-1 Revenue Bonds (Leveraged Bonds)	31,645,000	33,840,000
2009 Series DW-2 Revenue Bonds (Leveraged BAB Bonds)	31,400,000	31,400,000
2010 Series SRF-1 DW Revenue Bonds (State Match Bonds)	2,405,000	—
2010 Series SRF-1 DW Revenue Bonds (Leveraged Bonds)	59,105,000	—
2011 Series SRF Revenue Bonds (State Match Bonds)	3,500,000	—
2011 Series SRF Revenue Bonds (Leveraged Bonds)	49,880,000	—
Total bonds payable	287,305,000	276,465,000
Unamortized net original issue premium	10,521,338	6,705,488
Current maturities	(16,225,000)	(13,685,000)
Long Term Revenue Bonds payable, net	\$ 281,601,338	\$ 269,485,488

Long-term liability activity for the years end June 30, 2011 and 2010, respectively, were as follows:

	Beginning Balance	Additions	Reductions	Ending Balance	Due Within One Year
Revenue Bonds Payable	\$ 276,465,000	\$ 114,890,000	\$ (104,050,000)	\$ 287,305,000	\$ 16,225,000

	Beginning Balance	Additions	Reductions	Ending Balance	Due Within One Year
Revenue Bonds Payable	\$ 253,975,000	\$ 73,040,000	\$ (50,550,000)	\$ 276,465,000	\$ 13,685,000

The 2002 Series 1 Revenue Bonds (State Match Bonds), in the original amount of \$4,100,000, consist of a serial bond totaling \$175,000 as of June 30, 2011. The serial bond is due in an annual principal payment of \$175,000 with the final payment due April 1, 2012, and bears interest at 4.3%.

KANSAS PUBLIC WATER SUPPLY LOAN FUND
(AN ENTERPRISE FUND OF THE STATE OF KANSAS)

Notes To Financial Statements *(Continued)*

The 2002 Series 2 Revenue Bonds (Leveraged Bonds), in the original amount of \$47,705,000, consist of a serial bond totaling \$1,950,000 as of June 30, 2011. The serial bond is due in an annual principal payment of \$1,950,000 with the final payment due on April 1, 2012, and bears interest at 4.375%, payable semi-annually.

The 2004 Revenue Bonds, in the original amount of \$176,010,000, consist of serial bonds and a term bond totaling \$87,365,000 and \$11,270,000, respectively, as of June 30, 2011. The serial bonds are due in annual principal payments ranging from \$2,650,000 to \$14,520,000 with the final payment due on April 1, 2024, and bears interest at rates ranging from 3.25% to 5%, payable semi-annually. The term bond has one annual principal payment of \$11,270,000, bears interest at 4.625% payable semi-annually, and is due April 1, 2026.

The 2008 Revenue Bonds, in the original amount of \$36,700,000, consist of serial bonds totaling \$2,210,000 as of June 30, 2011. The serial bonds are due in annual principal payments ranging from \$1,010,000 to \$1,200,000 with the final payment due on April 1, 2013, and bear interest at 5%, payable semi-annually.

The 2009 Revenue Bonds were issued in the original amount of \$73,040,000 and consist of serial bonds, Series DW-1 and DW-2 totaling \$38,045,000 and \$29,980,000, respectively, and a Series DW-2 term bond totaling \$1,420,000, as of June 30, 2011. The Series DW-1 serial bonds are due in annual principal payments ranging from \$565,000 to \$9,750,000 with the final payment due on April 1, 2023, and bear interest at rates ranging from 1.5% to 3.25%, payable semi-annually. The Series DW-2 serial bonds are due in annual principal payments ranging from \$3,800,000 to \$7,195,000 with the final payment due on April 1, 2026, and bear interest at rates ranging from 4.8% to 5.2%, payable semi-annually. The DW-2 term bond has one annual principal payment of \$1,420,000, bears interest at 5.6% payable semi-annually, and is due April 1, 2029.

KANSAS PUBLIC WATER SUPPLY LOAN FUND
(AN ENTERPRISE FUND OF THE STATE OF KANSAS)

Notes To Financial Statements *(Continued)*

On December 15, 2010, the Series 2010SRF Revenue Bonds were issued in the original amount of \$213,950,000 for the Public Water Supply (PWS) and Water Pollution Control (WPC) Programs. The bonds consist of Series 2010SRF-1, which include both PWS and WPC, and Series 2010SRF-2 and 2010SRF-3, for WPC. The Public Water Supply portion of Series 2010SRF-1 were issued in the original amount of \$61,510,000 and consist of serial bonds totaling \$61,510,000, as of June 30, 2011. The Series 2010SRF-1 serial bonds are due in annual principal payments ranging from \$1,720,000 to \$10,700,000 with the final payment due on March 1, 2022, and bear interest at rates ranging from 2% to 5%, payable semi-annually. The proceeds from Series 2010SRF-1 provided \$2,656,444 from state match bonds, \$65,664,067 from leveraged bonds, and an amount required to pay costs of issuance. Bonds proceeds of \$68,320,511 and loan principal prepayments of \$33,709,341 were deposited in the 2010-1 PWS Drinking Water Escrow account to partially refund \$90,365,000 of the 2002 Series 1 and 2 Bonds, and the Series 2004 and 2008 leveraged bonds. An irrevocable escrow account with UMB Bank as escrow agent was established to provide amounts sufficient for payment of principal and interest on the refunded bonds. Accordingly, the escrow account and the refunded bonds are not included in the Fund's statement of net assets. This advance refunding was undertaken to reduce the total debt service payments, including interest, over the life of the debt by \$36,662,228. The refunding results in an economic gain (difference between the present value of the debt service payments of the refund and the refunding bonds) of \$11,585,875.

The refunding resulted in difference between the reacquisition price and the net carrying amount of the refunded debt of \$9,922,775. This difference will be reported in the accompanying financial statements as a deduction from bonds payable and will be charged to operations through the year 2023 using the straight-line method.

KANSAS PUBLIC WATER SUPPLY LOAN FUND
(AN ENTERPRISE FUND OF THE STATE OF KANSAS)

Notes To Financial Statements *(Continued)*

On May 24, 2011, the 2011SRF Revenue Bonds were issued in the original amount of \$53,380,000 and consist of serial bonds totaling \$53,380,000, as of June 30, 2011. The serial bonds are due in annual principal payments ranging from \$85,000 to \$7,805,000 with the final payment due on March 1, 2031, and bear interest at rates ranging from 2.00% to 4.20%, payable semi-annually. The proceeds provided \$3,500,000 of State match loan funds and \$49,500,000 of leveraged loan funds for the program and an amount required to pay the costs of issuance. The proceeds were used to provide funds to reimburse the general recycled loan account for project payments that were paid from the recycled account until the bonds were issued and to fund existing loan commitments.

The Master and Supplemental Bond Resolutions for the Bonds provide for the establishment of debt service reserve funds which are maintained and administered by KDFA. At June 30, 2011, the Fund was not in default of any provisions of the Master and Supplemental Bond Resolutions. The Master Financing Indenture provides for the establishment of a debt service reserve fund in the custody of the trustee in the name of the KDFA. At June 30, 2011, the Fund was not in default of any provisions of the Master Financing Indenture or the Supplemental Indenture.

Aggregate revenue bond debt service requirements are as follows:

Year Ending June 30,	Principal Amount Due	Interest Amount Due	Total
2012	\$ 16,225,000	\$ 12,514,899	\$ 28,739,899
2013	17,310,000	11,708,846	29,018,846
2014	18,130,000	10,891,503	29,021,503
2015	19,600,000	10,109,603	29,709,603
2016	21,450,000	9,177,590	30,627,590
2017 - 2021	77,885,000	34,650,962	112,535,962
2022 - 2026	86,400,000	17,960,225	104,360,225
2027 - 2031	30,305,000	3,300,200	33,605,200
	\$ 287,305,000	\$ 110,313,828	\$ 397,618,828

Certain of the above bonds may be redeemed prior to maturity in accordance with related bond indentures.

The debt service payment in FY 2011 was \$13,685,000 for principal with cumulative principal payments totaling \$94,220,000 and \$10,454,269 for interest with cumulative interest payments totaling \$119,898,979.

KANSAS PUBLIC WATER SUPPLY LOAN FUND (AN ENTERPRISE FUND OF THE STATE OF KANSAS)

Notes To Financial Statements *(Continued)*

The fund defeased certain State Revolving Fund revenue bonds by placing the proceeds for new bonds in an irrevocable escrow account with the Treasurer and UMB Bank to provide for all future debt service payments on the old bonds. Accordingly, the escrow account assets and the liability for the defeased bonds are not included in the Fund's financial statements. At June 30, 2011, \$115,460,000 of bonds have been defeased and are no longer included in bonds outstanding.

6. Arbitrage Rebate

In accordance with Internal Revenue Code Section 148(f) relating to arbitrage restrictions on tax-exempt bonds, there is currently no rebate liability for the Series 2002, 2004, 2008, 2009, 2010 and 2011 bonds as of June 30, 2011 and 2010.

7. Federal Capitalization Grants

As of June 30, 2011, the federal capitalization grants for 1997 through 2006 and the 2009 ARRA grant have been drawn down.

The 2007 federal capitalization grant of \$8,229,000 was awarded on June 8, 2007 with four percent, \$329,160, allocated for administration, \$225,000 reserved for technical assistance, and \$580,000 reserved for other authorized activities 1452K (1)b as evidenced by the budget page of the grant award. As program administration funds are earned, grant revenue is recognized. An amount of \$7,094,840 is reserved for the leveraged bond reserve account.

As of June 30, 2011, \$14,555 of the 2007 capitalization grant had not been drawn down. The entire 2007 capitalization grant has met the State matching requirements and is available based on the grant payment schedule.

The 2008 federal capitalization grant of \$8,146,000 was awarded on June 13, 2008 with 4%, \$325,840, allocated for administration, and \$225,000 reserved for technical assistance as evidenced by the budget page of the grant award. As program administration funds are earned, grant revenue is recognized. An amount of \$7,595,160 is reserved for the leveraged bond reserve account.

KANSAS PUBLIC WATER SUPPLY LOAN FUND
(AN ENTERPRISE FUND OF THE STATE OF KANSAS)

Notes To Financial Statements *(Continued)*

As of June 30, 2011, \$15,191 of the 2008 capitalization grant had not been drawn down. The entire 2008 capitalization grant has met the State matching requirements and is available based on the grant payment schedule.

The 2009 federal capitalization grant of \$3,491,000 was partially awarded on March 11, 2009 with four percent, \$139,640, allocated for administration, \$156,900 reserved for technical assistance, and \$349,100 for State program management as evidenced by the budget page of the grant award. As program administration funds are earned, grant revenue is recognized. An amount of \$2,845,360 is reserved for the leveraged bond reserve account.

On September 4, 2009, the balance of the 2009 capitalization grant, \$4,655,000 was awarded with four percent, \$186,200, allocated for administration, \$90,520 reserved for technical assistance, and \$50,900 for State program management as evidenced by the budget page of the grant award amendment. As program administration funds are earned, grant revenue is recognized. An amount of \$4,327,380 is reserved for the leveraged bond reserve account.

As of June 30, 2011, \$722,835 of the 2009 capitalization grant had not been drawn down. The entire 2009 capitalization grant has met the State matching requirements and is available based on the grant payment schedule.

The 2010 federal capitalization grant of \$16,605,000 was awarded on November 8, 2010 with four percent, \$664,200, allocated for administration, \$332,100 reserved for technical assistance, and \$850,000 for other authorized activities as evidenced by the budget page of the grant award. As program administration funds are earned, grant revenue is recognized. An amount of \$14,758,700 is reserved for direct loans.

On December 6, 2010, an amendment was processed that revised the programmatic terms and conditions which included fringe benefits but did not change the grant amount, direct loan, or set-aside amounts.

As of June 30, 2011, \$15,310,627 of the 2010 capitalization grant had not been drawn down. The entire 2010 capitalization grant has met the State matching requirements and is available based on the grant payment schedule.

KANSAS PUBLIC WATER SUPPLY LOAN FUND
(AN ENTERPRISE FUND OF THE STATE OF KANSAS)

Notes To Financial Statements *(Continued)*

Federal capitalization grants awarded by the EPA through June 30, 2011 are as follows:

Federal Fiscal Year	Loans	Reserve	Program Administration	Other Set-Asides	Total Grant
1997 Grant Award	\$ —	\$ 11,776,871	\$ 563,800	\$ 1,754,329	\$ 14,095,000
1998 Grant Award	—	9,407,614	400,324	200,162	10,008,100
1999 Grant Award	—	9,860,036	419,576	209,788	10,489,400
2000 Grant Award	—	10,393,127	436,060	72,313	10,901,500
2001 Grant Award	—	9,969,176	436,190	541,234	10,946,600
2002 Grant Award	—	9,001,632	—	233,068	9,234,700
2003 Grant Award	—	8,812,032	367,168	—	9,179,200
2004 Grant Award	—	9,141,216	380,884	—	9,522,100
2005 Grant Award	—	7,934,148	751,138	816,614	9,501,900
2006 Grant Award	—	7,310,128	329,172	590,000	8,229,300
2007 Grant Award	—	7,094,840	329,160	805,000	8,229,000
2008 Grant Award	—	7,595,160	325,840	225,000	8,146,000
2009 Grant Award	—	7,172,740	325,840	647,420	8,146,000
2009 Grant-ARRA	19,500,000	—	—	—	19,500,000
	19,500,000	115,468,720	5,065,152	6,094,928	146,128,800
Less cumulative amounts drawn down	(9,454,511)	(115,468,720)	(4,286,112)	(5,096,707)	(134,306,050)
	10,045,489	—	779,040	998,221	11,822,750
2010 Grant Award	14,758,700	—	664,200	1,182,100	16,605,000
Less amounts drawn down during Fiscal Year 2011	(11,064,297)	—	(440,405)	(859,841)	(12,364,543)
	\$ 13,739,892	\$ —	\$ 1,002,835	\$ 1,320,480	\$ 16,063,207

As of June 30, 2011 and 2010, \$16,063,207 and \$11,822,750, respectively, of the capitalization grants had not been drawn down.

8. State Capital Contributions

On July 30, 1998, the Fund received a deposit of \$1,000,000 per K.S.A. 74-8203, as amended and supplemented. On July 30, 1999, the Fund received a deposit of \$4,000,000, which represents the balance of the anticipated State contribution. The State contribution is to be used to further leverage the program through the issuance of additional revenue bonds.

**Independent Accountants' Report On Internal Control Over
Financial Reporting And On Compliance And Other Matters
Based On An Audit Of The Financial Statements Performed In
Accordance With *Government Auditing Standards***

Dr. Robert Moser, MD
Secretary of Kansas Department of Health and Environment and the
Board of Directors of the Kansas Development Finance Authority
Topeka, Kansas

We have audited the financial statements of the Kansas Public Water Supply Fund (the Fund) as of and for the year ended June 30, 2011 and have issued our report thereon dated January 27, 2012, which contained a reference to the reports of other auditors. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the Fund's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Fund's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the Fund's internal control over financial reporting.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis. A material weakness is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. We consider the deficiency described in the accompanying schedule of findings and responses as item 2011-2 to be a material weakness.

Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be deficiencies, significant deficiencies or material weaknesses. However, as described in the accompanying schedule of findings and responses, we identified a deficiency in internal control over financial reporting that we consider to be a material weakness, as defined above. In addition, we identified a deficiency in internal control over financial reporting, described in the accompanying schedule of findings and responses as item 2011-1, that we consider to be a significant deficiency. A significant deficiency is a deficiency, or combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit the attention of those charged with governance.

Compliance And Other Matters

As part of obtaining reasonable assurance about whether the Fund's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

The Fund's responses to the findings identified in our audit are described in the accompanying corrective action plan. We did not audit the Fund's responses and, accordingly, we express no opinion on them.

This report is intended solely for the information and use of the Kansas Department of Health and Environment, the Board of Directors of the Kansas Development Finance Authority, management of the Fund and the Environmental Protection Agency and is not intended to be and should not be used by anyone other than these specified parties.

RubinBrown LLP

Overland Park, Kansas
January 27, 2012

**KANSAS PUBLIC WATER SUPPLY LOAN FUND (AN
ENTERPRISE FUND OF THE STATE OF KANSAS)**

SCHEDULE OF FINDINGS AND RESPONSES

June 30, 2011

Finding No. 2011-1 - Significant Deficiency

Condition - Throughout the year, the Fund's journal entries and financial statements were not being reviewed by someone other than the preparer.

Cause - The internal control system over financial reporting did not function as designed. The design included a review of journal entries and financial statements. The management of the Fund is responsible for establishing and maintaining a system of internal controls. The objective of an internal control system is to provide management with reasonable, but not absolute, assurance that transactions are executed in accordance with management's authorization and recorded properly to permit the preparation of financial statements.

Effect - There is a potential that the financial statements may be materially misstated.

Recommendation - We recommend that the internal control system over financial reporting be followed including review of the financial statements and journal entries that support the financial statements.

Management's Response/Corrective Action Plan (Unaudited) - The Office of Management Analysis and Standards agrees with the observation and acknowledges this as a recurring issue from the fiscal year 2010 audit report.

Efforts to satisfy this observation were not sufficient over the past year and were not fully documented for auditor review. The Office of Management Analysis and Standards is working to develop and implement a formal review process to meet the financial reporting internal control standards.

Completion Date: April 30, 2012

Contact Person and Title: Martin Eckhardt, Director, Office of Management Analysis and Standards

KANSAS PUBLIC WATER SUPPLY LOAN FUND (AN ENTERPRISE FUND OF THE STATE OF KANSAS)

Schedule Of Findings And Responses (*Continued*)

Finding 2011-2 - Material Weakness

Condition: Internal controls over the reconciliation of the pooled cash operating account at the State of Kansas (State) were not properly modified and implemented upon conversion to the new general ledger software package (SMART).

Cause: The State converted to SMART at the beginning of the fiscal year. The conversion changed the type and level of detail of the information that was previously provided to perform the reconciliation. The bank reconciliation procedures and related controls were not reviewed and modified timely to allow for bank reconciliations to be performed accurately throughout the year.

Effect: At fiscal year-end, the State tried to prepare a bank reconciliation for the entire fiscal year. The State was unable to reconcile cash timely and accurately and had to revisit reporting information produced from their general ledger to determine that the integrity of the information being produced and used for the bank reconciliation had remained intact. This exercise discovered conversion issues that needed to be corrected in order to reconcile properly. This process should have been performed and procedures and controls adjusted as close to the conversion date as possible.

Recommendation: We recommend that management formalize the new processes and procedures and perform bank reconciliations for the pooled operating account on a monthly basis going forward.

Management's Response/Corrective Action Plan (Unaudited): The Department of Administration and the Office of the State Treasurer agree with this finding. The formal procedures for the reconciliation of the State Treasurer's common cash and investment accounts to the SMART accounting records were not fully developed and implemented prior to July 1, 2010. One result was that it took an extended period of time to pull together the records for the auditor in order to reconcile the SMART cash balances with the State Treasurer's bank balances.

Over the past few months, joint efforts of the Department of Administration and the Office of the State Treasurer have resulted in significant progress in developing the formal reconciliation procedures and processes that will be used on a monthly basis prospectively. We anticipate the procedures will be completed by April 30 and fully implemented by end of fiscal year 2012.

Completion Date: June 30, 2012

Contact Person and Title: Martin Eckhardt, Director, Office of Management Analysis and Standards

**KANSAS PUBLIC WATER SUPPLY LOAN FUND
(AN ENTERPRISE FUND OF THE STATE OF KANSAS)**

**SUMMARY SCHEDULE OF PRIOR YEAR AUDIT FINDINGS
June 30, 2011**

Finding No. 2010-1 - (Repeated, See 2011-1)

Condition - Throughout the year, the Fund's journal entries and financial statements were not being reviewed by someone other than the preparer.

Finding repeated in the current year, see 2011-1.